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June 29, 1994

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JUN 29 1994

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

William F. Caton  
Secretary  
Federal Communications Commission  
1919 M Street, N.W. Room 222  
Washington, DC 20554

Re: CC Docket No. 94-1  
Price Cap Performance Review  
for Local Exchange Carriers

Dear Mr. Caton:

Enclosed herewith for filing with the Commission are an original and four (4) copies of the Reply Comments of the Computer & Communications Industry Association in the above-captioned docket. This filing is made pursuant to Section 1.419 of the Commission's rules, 47 C.F.R. § 1.419. Please direct any questions regarding this filing to the undersigned.

Very truly yours,

*Charles A. Zielinski*  
Charles A. Zielinski

Enclosures

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**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

**In the Matter of**

**Price Cap Performance Review  
for Local Exchange Carriers**

CC Docket No. 94-1

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**JUN 29 1994**

**REPLY COMMENTS OF THE  
COMPUTER & COMMUNICATIONS INDUSTRY ASSOCIATION  
ON PROPOSED RULEMAKING**

FEDERAL COMMUNICATIONS COMMISSION  
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**DATED: June 29, 1994**

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### SUMMARY

In these reply comments, CCIA continues to support the price cap regulatory option for LECs which CCIA outlined in its initial comments. Under that plan, participating LECs would receive more favorable price cap regulatory treatment in return for providing inside wire facilities to public schools and libraries in their service territories. As clarified herein, the plan would require LECs to propose and support both the amount and form of the benefit to be received. However, the Commission should not, and could not lawfully mandate an LEC to adopt CCIA's plan.

CCIA also supports reform of the basic price cap regulatory system. Even if the Commission chooses to retain "sharing" as part of the system, despite the flaw it creates, there is good reason to deregulate LEC depreciation rates. That initiative would promote more LEC network investment, including investment in the advanced technologies necessary to build out the National Information Infrastructure.

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**Before the  
Federal Communications Commission  
Washington, D.C. 20554**

<div style="display: flex; justify-content: space-between; align-items: center;"><div style="width: 80%;">In the Matter of</div><div style="width: 10%; text-align: center;">)</div><div style="width: 10%;"></div></div> <div style="display: flex; justify-content: space-between; align-items: center;"><div style="width: 80%;">Price Cap Performance Review for Local Exchange Carriers</div><div style="width: 10%; text-align: center;">)</div><div style="width: 10%;"></div></div>	) CC Docket No. 94-1 ) ) ) )
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**REPLY COMMENTS OF THE  
COMPUTER & COMMUNICATIONS INDUSTRY ASSOCIATION  
ON PROPOSED RULEMAKING**

**I. INTRODUCTION**

In its initial comments of May 9, 1994 on the Commission's Notice of Proposed Rulemaking in the above-captioned docket, the Computer & Communications Industry Association ("CCIA") showed that the existing scheme of price cap regulation for LECs, because it includes "sharing" and depreciation regulation, fails to provide the strongest possible positive financial incentives for local exchange carrier ("LEC") investment in advanced telecommunications infrastructure. CCIA also demonstrated that there is a particularly strong national interest in the development of such an infrastructure for primary and secondary public schools, as well as for public libraries.<sup>1</sup> The Council of Chief State School Officers, and the National Association of Secondary School Principals also emphasized that strong national interest in their initial comments. As far as CCIA can determine, the initial comments of other parties did not

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<sup>1</sup> CCIA Comments at 6-13.

address the need for providing stronger LEC incentives targeted to the development of the telecommunications infrastructure for the education sector of the economy.

In its initial comments, CCIA outlined an optional program under price cap regulation to promote the rapid wiring up of schools and libraries for telecommunications. CCIA specifically proposed that the Commission offer LECs more favorable treatment under price cap regulation in return for providing advanced inside wire facilities to the Nation's two million public school classrooms, as well as to its public libraries.<sup>2</sup> Such facilities are essential to interactive communications and the effective use of multimedia software to achieve improvements in education; yet only about 12 percent of the Nation's classrooms currently are equipped with a telephone line.<sup>3</sup>

Under CCIA's policy option, an LEC would submit a plan to the FCC, subject to its approval, with a fixed time period and annual goals for wiring up public schools and libraries in its service territories. In return for achieving an annual goal, the LEC would receive more favorable price cap regulatory treatment in its current price cap review period. CCIA continues to urge adoption of its proposed policy option.

In these reply comments, CCIA will further explicate and clarify its proposal in order to resolve three issues that have arisen with respect to its plan. Those issues are:

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<sup>2</sup> Id. at 13-16.

<sup>3</sup> Id. at 14.

(a) whether the plan should or could be mandated for all LECs; (b) how the amount of the benefit to an LEC under the plan should be determined; and (c) how the particular form of price cap regulation relief for an LEC should be determined. As CCIA explains in the discussion below, its plan should not and cannot be mandated for all LECs. Furthermore, an LEC should be required to propose and reasonably support the amount of the benefit it would receive in relation to its contribution to education sector infrastructure development in a formal written submission to the FCC. A participating LEC should also be permitted to state its own preferred form of relief, and the Commission should grant both the amount and form of relief proposed by an LEC which has properly supported its request.

CCIA also replies to certain initial comments on reforms to basic price cap regulation for LECs. Like CCIA, other parties have observed that "sharing" tends to undermine the efficiency goal of price cap regulation. However, should the Commission decide to retain "sharing" at this time in order to maintain LEC rate of return regulation, it should at least deregulate LEC depreciation rates. That initiative alone, as CCIA explains herein, would stimulate more LEC investment in regulated local network plant and thus promote completion of the National Information Infrastructure ("NII"). That is a primary goal on which the newly constituted Commission should focus its policy initiatives.

## II. DISCUSSION

This proceeding presents the newly constituted Commission with a crossroads in price cap regulation policy. The Commission may, in effect, adopt the existing policy by making little or no changes to it. That policy does not contain the strongest possible incentives to LECs to invest in the NII. Or the Commission may promulgate major reforms to price cap regulation that create, in effect, a new policy that more effectively stimulates LEC investment in the NII. CCIA favors the latter course of action.

CCIA's members include both major telecommunications and computer companies. CCIA's policy option is designed to serve the interests of its members as well as the national interest in improved education. CCIA's computer company members are willing and able to provide the applications of computer technology in schools and libraries that are needed to achieve advancement in education. At a minimum, however, these applications require appropriate inside wire facilities to connect computers to telecommunication networks. CCIA's policy option would create strong incentives for LECs to install such facilities and would thus serve the national interest in educational improvement.

CCIA's members also have an interest in the rapid deployment of advanced telecommunication technologies in LEC network plant. Such improvements would facilitate the wider use of computer technology in schools, libraries, and elsewhere. They would build out the NII, whose economic

benefits to the Nation as a whole have been well documented.<sup>4</sup> For these reasons, CCIA supports basic price cap regulatory reforms that would strengthen LEC incentives to invest in network plant improvements. Deregulation of LEC depreciation rates is one such reform that CCIA would support.

**A. CCIA's Policy Option for Price Cap Regulated LECs**

**1. CCIA's Proposal Can and Should Be Adopted Only as an Option for LECs under Price Cap Regulation**

In its initial comments, CCIA clearly stated that its plan should be adopted only as an option for LECs.<sup>5</sup> As a matter of sound public policy, the Commission should not mandate that all LECs follow CCIA's plan because the plan cannot work without the willing and active cooperation of an LEC. CCIA's plan contemplates that an LEC will eagerly negotiate an agreement with schools and libraries for the installation of inside wire facilities. An unwilling LEC that is participating in the plan only because of an FCC mandate is unlikely ever to reach such an agreement. Thus, the FCC should provide a reasonable incentive for an LEC to participate in the plan, but it should not mandate participation.

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<sup>4</sup> See, e.g., Economic Benefits of the Administration's Legislative Proposals for Telecommunications, Council of Economic Advisors (June 14, 1994).

<sup>5</sup> Id. at 16. CCIA has also fashioned its proposal only for LECs. If other possible providers of inside wire facilities for schools and libraries show a compelling interest that has yet to surface, revisions to the plan may be needed.

Moreover, beyond these practical policy concerns, it would be unlawful for the Commission to order all LECs to adopt CCIA's proposal. Under that plan, LECs would supply inside wire facilities to public schools and libraries. The Commission deregulated the LEC's provision of those facilities some time ago.<sup>6</sup> Mandating that all LECs enter into contracts with public schools and libraries to provide those services could constitute unreasonable and therefore unlawful reimposition of federal regulation of inside wire facilities. The problem is not that prices for inside wiring are non-competitive and need to be regulated. Rather the problem, which CCIA's plan addresses, is the apparent lack of financial resources for public schools and libraries to pay for the cost of inside wire facilities. The existence of that problem provides no reasonable basis for reimposing regulation, in any form, on the LECs' provision of inside wire facilities.

However, the Commission can, under CCIA's proposal, offer to enter into "social contracts" with LECs under which the Commission would provide price cap regulatory relief in return for an LEC's voluntary fulfillment of a commitment to wire up public schools and libraries in its service territories on an approved schedule. Such agreements would further FCC public policy goals. But no LEC would be directed to enter into such agreements.

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<sup>6</sup> See Detariffing the Maintenance and Installation of Inside Wire, Reconsideration Order, 51 Fed. Reg. 8498 (1986), further reconsideration, 3 FCC Rcd. 1719 (1988) remanded National Assn. of Regulatory Utility Comm'rs. v. F.C.C., 880 F. 2d 422 (D.C. Cir. 1989), on remand, 7 FCC Rcd. 1334 (1992).

2. A Participating LEC Would Propose and Support the Amount of Its Benefit Under CCIA's Plan

In its initial comments CCIA made clear the obligations of an LEC that chose to participate in the CCIA plan. The LEC would be required to enter into agreements with appropriate local officials in its service territories to wire up mutually agreed upon classrooms and other spaces in the public schools and the public libraries for telecommunications services. The LEC would also establish a schedule for completing the task. That schedule would be submitted to the FCC for its approval. An LEC would have to meet the annual targets in its approved schedule to earn its annual relief from whatever form of price cap regulation remains at the conclusion of this proceeding.<sup>7</sup>

CCIA did not specify in its initial comments the amount of benefit that an LEC should receive as relief from price cap regulation. Under the plan, however, it is unnecessary for the Commission to specify the precise amount of benefit to an LEC in advance. The Commission should establish, of course, that the benefit, at a minimum, would be sufficient to compensate an LEC for its unrecovered costs of participating in the plan. Such unrecovered costs could include inside wire facilities and installation costs, the cost of negotiating agreements, and associated costs. The Commission, however, should require each participating LEC to propose in its

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<sup>7</sup> CCIA's proposal, however, is not so rigid as to preclude any relief to an LEC that, for example, wired up 99 out of 100 classrooms on schedule. An LEC that showed good cause for falling short of its commitment in a given annual period should receive regulatory relief.

written submission to the agency a benefit amount, and to provide support for its proposed amount.

Under this approach, each LEC would be able to propose an amount of benefit based on its own individual facts and circumstances. Some LECs, for example, might have to expend more resources than others to negotiate agreements and fulfill their commitments on schedule. LECs may thus be able to justify a greater benefit, and they would be allowed to do so under CCIA's proposal.

3. A Participating LEC Would Propose and Support its Preferred Form of Relief Under CCIA's Plan

In its initial comments CCIA did not specify the precise form of relief from price cap regulation that should be accorded to an LEC. CCIA pointed out, as an example, that an LEC could be relieved of the "consumer productivity dividend" ("CPD") portion of the prevailing productivity factor.<sup>8</sup> However, as other parties have noted in their initial comments, the Commission added the CPD to the baseline productivity factor mainly to heighten the hurdle LECs would have to clear in order to achieve additional returns for their shareholders under price cap regulation in the initial years.<sup>9</sup> The Commission now has experience with productivity improvement under price cap regulation and may, for that

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<sup>8</sup> CCIA Comments at 15.

<sup>9</sup> See e.g., Policy and Rules Concerning Rates for Dominant Carriers, Second Further Notice of Proposed Rulemaking, 4 FCC Rod 2873, 3223 (1989).

reason, choose to specify a productivity factor that does not include an additional CPD.

Moreover, some parties have argued in their initial comments that the Commission should eliminate "sharing" and, therefore, depreciation regulation from its price cap scheme.<sup>10</sup> These parties contend that the Commission should confine price cap regulation to prices. Under these proposals, the Commission would, in effect, eliminate rate of return regulation.

Without knowing what form price cap regulation will take at the conclusion of this proceeding, CCIA is unable to recommend a particular form of price cap regulatory relief for LECs under its plan. However, the merits of CCIA's plan do not depend on a particular form of relief. The plan simply requires relief for LECs from federal price cap regulation in some form that is sufficient to provide a benefit to an LEC commensurate with the benefit it confers through wiring up the public school classrooms and libraries in its service territory.

Accordingly, CCIA's plan contemplates that an LEC would propose not only the amount of the benefit it should receive, but also the form of that benefit, in its formal written submission to the FCC. At that time, an LEC will be in a position to propose relief on the basis of any revisions to basic price cap regulation the Commission may adopt in this

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<sup>10</sup> See e.g., Comments of the United States Telephone Association ("USTA"), Attachment 1 at 5.

proceeding. The LEC would be obligated to provide reasoned support for both the amount and form of the benefit it proposes. Unless the Commission had reason to question the form of relief proposed, the LEC would receive relief in the form it prefers.

An LEC would also have an obligation to demonstrate that the particular form of relief it proposed equated to the amount of benefit it proposed. The Commission would thus receive sufficient information to assure that a participating LEC would not acquire, by means of the form of relief from price cap regulation that it proposed, more or less than the benefit the LEC had justified.<sup>11</sup>

**B. Deregulation of Depreciation Rates As a Basic Price Cap Regulatory Policy Reform**

While CCIA's price cap policy option would promote wiring up public schools and libraries, the basic price cap regulatory scheme must serve to stimulate LEC investment in advanced local network technology that can be effectively used not only by the education sector, but also other sectors of the economy that rely on computers and telecommunications facilities. USTA, among others, has argued that the Commission should eliminate "sharing" and, as a consequence,

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<sup>11</sup> For example, if the form of relief were a reduction in the "sharing" obligation, the LEC would equate the amount of its benefit to the same amount of revenue it would otherwise be required to give to its interexchange carrier customers.

depreciation regulation from the price cap regulatory scheme.<sup>12</sup> However, even if the Commission is not inclined to eliminate "sharing" at this time, there are good reasons to deregulate LEC depreciation rates.

As CCIA pointed out in its initial comments, depreciation regulation is far from an exact science and the Commission is no longer regulating a monopoly LEC industry. Under conditions of monopoly and restricted entry, it may be possible to delay deployment of new technology until older technology is fully depreciated according to the "life" for that equipment established by regulators. Competitive forces, however, now bring new technology to the market more rapidly and render old technology economically obsolete, regardless of the "life" for that equipment determined by regulation. The Commission can neither accurately predict nor establish the time of economic obsolescence under competitive conditions.

In addition, depreciation regulation produces false results under a price cap regulation scheme that includes "sharing." An LEC that wants to accelerate depreciation on existing plant may be prevented from doing so by FCC regulation. In such cases, the LEC's depreciation expense and, therefore, its total expenses are artificially lowered for regulatory purposes. As a result, the rate of return on investment for regulatory purposes is higher and may reach a level that requires "sharing" solely because of regulation of an LEC's depreciation rates.

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<sup>12</sup> See Comments of USTA, Attachment 1 at 5.

Moreover, an LEC that accelerates depreciation reduces its investment base and, therefore, all other things being equal, creates a higher rate of return that may be subject to "sharing." In order to avoid "sharing," an LEC would have to increase its investment base. Thus, accelerated depreciation in a "sharing" environment would promote more LEC investment in network plant, including the advanced network technologies necessary to build out the NII.

To the extent that "sharing" now occurs solely because of depreciation rate regulation, an LEC is forced, in effect, to transfer revenues to interexchange carrier customers that the LEC could otherwise retain for reinvestment in advanced local network technology. Thus, depreciation regulation may hinder LEC efforts to build the local pieces of the NII. FCC policy should now be designed to promote effectively rather than possibly hinder LEC efforts to build the NII.<sup>13</sup>

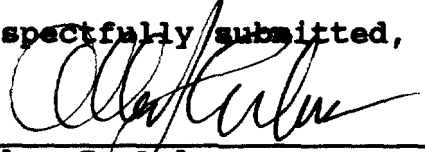
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<sup>13</sup> Although state commissions are not obligated to conform to FCC depreciation policy for LECs under current law, an FCC initiative to accelerate depreciation may well induce many state commissions to take similar action in support of the NII.

### III. CONCLUSION

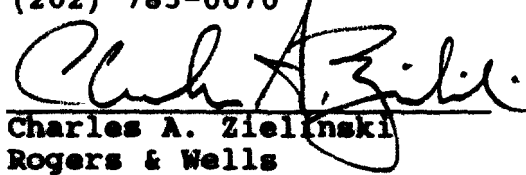
With the clarifications stated herein, CCIA urges the Commission to adopt the proposed option for price cap regulation outlined in CCIA's initial comments in this proceeding. That plan will serve the national interest by providing reasonable incentives to LECs to wire up the Nation's public schools and libraries for advanced telecommunications, and thereby lay the foundation for improvements in education that will benefit the entire economy. CCIA further urges the Commission, whether or not it eliminates "sharing," to promote accelerated depreciation of old LEC network plant technology in order to stimulate LEC investment in advanced network technology.

Respectfully submitted,



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Attorneys for  
Computer & Communications  
Industry Association

DATED: June 29, 1994

**CERTIFICATE OF SERVICE**

I do hereby certify that I caused a copy of the Reply Comments of the Computer & Communications Industry in CC Docket 94-1 to be served on the officials below by hand on this 29th day of June, 1994.

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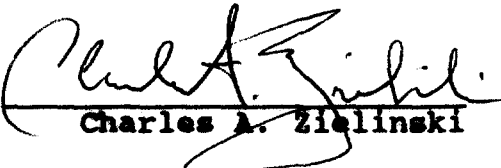
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